No. 5726.

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IN THE

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

In the Matter of
JAMESON & MEYERS,
Bankrupts.

Pauley Oil Company,
Appellant,
vs.
E. A. Lynch, Trustee in Bankruptcy of the Estate of Robert F. Meyers and Claude S. Jameson, doing business under the firm name of Jameson & Meyers, and under the fictitious name of Eagle Gasoline Company,
Appellee.

APPELLANT'S BRIEF.

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APPELLANT'S BRIEF.

I. Introductory Statement.

This is an appeal from an order disallowing appellant's claim for $25,635.47 against the estate of the bankrupts. The order is based upon a finding that appellant

had received a voidable preference in the sum of $9100.00 which it had failed and refused to surrender.

The proceedings had in this matter prior to this appeal may be briefly stated in the following chronological order:

February 13, 1926, the creditors' petition for adjudication of bankruptcy was filed [Tr. p. 21], and thereafter, in due course, bankruptcy was adjudicated and the matter was referred to Earl E. Moss, Esq., referee in bankruptcy.

April 29, 1926, appellant filed the claim involved in this appeal. [Tr. pp. 3-10.]

June 26, 1926, said claim was approved and allowed by the referee.

July 19, 1927, the trustee's petition for a reconsideration of said claim was filed. [Tr. pp. 11-13.]

July 30, 1927, appellant's answer to said petition was filed. [Tr. pp. 13-20.]

July 3, 1928, the referee made his findings of fact and conclusions of law and an order disallowing the claim. [Tr. pp. 20-29.)

July 12, 1928, appellant filed its petition for review of the referee's order. [Tr. pp. 29-38.]

July 25, 1928, the referee made his supplemental findings of fact and conclusions of law. [Tr. pp. 38-41.]

November 8, 1928, the Hon. Wm. P. James, judge of the United States District Court, made his order on petition for review approving and confirming the order of the referee. [Tr. pp. 66-67.]

It will be noted that the referee made two sets of findings of fact. In his Referee's Certificate on petition for review he explains this anomaly in these words:

> "That in the course of the proceedings certain findings of fact and conclusions of law, together with an order thereon, were, by counsel for the trustee, presented to the referee, and apparently without a reading thereof inadvertently signed and filed by the referee. Upon the filing of the petition for review and the exceptions noted therein to the findings, the referee for the first time observed that such findings contained *much surplusage and statements of evidence* in lieu of ultimate facts, and the referee thereupon, on his own motion, prepared and filed supplemental findings of fact and order." [Tr. p. 42.] (Italics ours.)

Nevertheless, he attempted to justify each finding complained of by appellant, or dismissed it with the statement that it constituted "a statement of evidence immaterial to the decision and improperly made a part of the findings." [Tr. pp. 55-66.] We propose to show that instead of containing "statements of evidence," the original findings contain numerous *misstatements of evidence,* and that the referee's attempted justification is in part an unwilling confession of error and in part a misstatement of the evidence in this, that he selected certain evidence of events and conversations which on its face would indicate that appellant, at the time it received the payments which constitute the alleged voidable preference, knew or had reasonable cause to believe that the bankrupts were then insolvent without quoting the evidence which shows that these events and conversations took place after the last payment was received.

Furthermore, the referee can hardly escape responsibility for the findings, for almost without exception they find their source and authority in his opinion. [Tr. pp. 44-54.] Even if most of the findings complained of con-

stitute surplusage in that they go beyond formal findings upon the issues as pleaded, the assignments of error cannot for that reason be dismissed. They concern events and circumstances which the referee would have been compelled to take into consideration in making findings limited to the allegations of the pleadings. If he was in error in his findings upon these events and circumstances, it certainly is not improbable that he was in error in his ultimate conclusion.

II. The Issues.

On August 13, 1925, appellant entered into a written contract [Exhibit B, Tr. pp. 115-123] with Robert F. Meyers, one of the bankrupts (this contract was immediately thereafter assigned to Jameson & Meyers, the bankrupts herein), pursuant to which appellant sold and delivered gasoline to the bankrupts from August 13 to and including October 7, 1925, to the amount and value of $46,653.82. [Tr. pp. 3-10.] Upon this account the bankrupts paid in all $22,500. (Id.) All of this sum was paid more than four months prior to bankruptcy, and it is not claimed that any part of it constituted a voidable preference. On or about August 13, 1925, appellant entered into an oral contract with Robert F. Meyers (which contract was also immediately assigned to Jameson & Meyers) pursuant to which it sold fuel oil to the bankrupts and delivered it upon their order to Los Angeles Gas & Electric Corporation, hereinafter called "the Gas Company." Shipments of fuel oil were made from appellant's refinery from August 14 to and including August 31, 1925. On October 13, 1925, being exactly four months prior to bankruptcy, there remained unpaid on ac-

count of this fuel oil the sum of $14,481.65. This amount was then evidenced by a trade acceptance. [Exhibit D, Tr. p. 125.] Thereafter the bankrupts made eleven payments totaling $13,000, all of which appellant applied upon the trade acceptance. [Tr. pp. 3-10, 105.] The unpaid balance on the gasoline account plus the unpaid balance on the trade acceptance, a total of $25,635.47, constitutes appellant's claim against the bankrupts' estate.

The referee found that during the entire time that the eleven payments totaling $13,000 were made and received, appellant knew or had reasonable cause to believe that the bankrupts were insolvent and that a preference would be effected, and that the said payments constituted a voidable preference to the extent and in the amount of $9100. [Original Findings, Tr. p. 26; Supplemental Findings, Tr. p. 41.]

The all-inclusive issues on this appeal are:

1. Did appellant at the times it received the said eleven payments, or any of them, have actual knowledge that thereby a preference would be effected? or,

2. If appellant did not then have such actual knowledge, did it then have reasonable cause to believe that thereby a preference would be effected?

Adverse findings upon the foregoing questions were assigned as error in the 17th assignment of error in the original findings [Tr. p. 133], the 2nd assignment of error in the supplemental findings [Tr. p. 135] and in the 3rd, 4th and 5th assignments of error in the referee's order [Tr. p. 136].

We have assigned as error numerous findings in regard to events and circumstances upon which the referee, we must assume, at least in part based his conclusions of law and order.

To review these findings in detail at this time would serve no useful purpose, but we shall call attention to the various assignments of error therein in our review of the evidence. We freely admit that some of the assignments of error, even if conceded, as for instance our second and third assignments of error in the original findings [Tr. p. 128], are of little consequence. When, however, we found that the original findings were erroneous in so many instances we felt impelled to point out all of the errors that came to our attention.

The principles of law applicable to the issues here involved are quite simple and universally recognized. The task before us is to sift from the record the facts actually supported and warranted by that record. This task would have been an easy one had Robert F. Meyers, one of the bankrupts, and the principal witness for the trustee, been candid and direct in his answers to the questions put to him. The character of this witness will appear in our statement of the case. Suffice it here to say that the discursive nature of his testimony has made the presentation of the case an ardous task and necessitates an unusually detailed review of the evidence. We feel that the amount involved in this controversy justifies such a review, and, while our statement of the case is extended, we trust that it will assist the court in ascertaining the actual facts.

At the outset we wish to state that we are fully cognizant of the rule that an appellate court will not disturb findings of fact made by the trial court unless such findings are not supported by any satisfactory evidence. In writing this brief, therefore, we shall evade no evidence favorable to appellee,—we shall make an honest endeavor to present the case in the light most favorable to him. We shall concede every point supported by any credible and satisfactory evidence, but we shall not concede any point merely because some evidence, which, when wrenched from its context, might be said to support the order complained of.

An inconsequential error, traceable in the first instance to the opinion of the referee, crept into the findings of fact and into the assignments of error. The merchandise sold by appellant to the bankrupts and delivered to the Gas Company is in the opinion, the original findings and in the assignments of error described as *crude* oil, whereas it should have been described as *fuel* oil.

III. Statement of the Case.

Appellant, Pauley Oil Company, is now, and at all times herein mentioned was, a California corporation. During the time of the transactions involved in this proceeding it was a small company and operating on limited capital. [Tr. p. 105.] Its president and general manager was E. L. Pauley. Its secretary was M. O. Sohus. Mr. Pauley testified that he and Mr. Sohus were the only officers or agents of Pauley Oil Company who had any dealings or transactions with the bankrupts [Tr p. 83], and his testimony is amply supported by the entire record.

Of the two bankrupts, Robert F. Meyers was the dominant figure. Claude S. Jameson did not testify or otherwise appear in this proceeding, and the record discloses little concerning him. Apparently both Mr. Meyers and Mr. Jameson had been in the gasoline retail business for some time before their dealings with appellant commenced. These dealings commenced in August, 1925. It was about this time that the partnership of Jameson & Meyers was formed. Mr. Meyers owned ten or eleven gasoline service stations while Mr. Jameson owned a number of service stations which he had operated under the name of Eagle Gasoline Company. When the partnership was formed these assets were merged under one management. Speaking of the volume of business done by this partnership, Mr. Meyers testified:

> "I was a bigger competitor of the Standard Oil Company in the same class of business than the Pauley Oil Company was at the time (September, 1925). Our average monthly sales of gasoline at that time amounted to altogether about $450.000." [Tr. pp. 107-108.]

During the time of his dealings with appellant, Mr. Meyers had occasion to buy crude oil; he bought "more than a million dollars worth." [Tr. p. 109.]

The Triangle Service Stations are mentioned frequently in the testimony. These stations belonged so far as the testimony in this proceeding goes, to Rosabelle Meyers, wife of Robert F. Meyers.

Mr. Pauley had known Mr. Meyers as early as 1922. Mr. Meyers was then engaged in the service station business. In 1923 Mr. Pauley entered negotiations with Mr. Meyers for the sale of gasoline to Mr. Meyers for the

Triangle Service Stations. These negotiations were unsuccessful but the reason for their failure does not appear in the record. [Tr. pp. 81, 93.] Mr. Pauley had not met Mr. Jameson until at the time of, or shortly after the transactions involved in this appeal commenced. [Tr. pp. 85, 87.] Mr. Pauley testified:

> "At that time (just prior to the making of the contracts) I didn't know much about Jameson & Meyers being only in existence for about 6 months. The contract was made with Mr. Meyers and I didn't know much about Jameson. He (Mr. Meyers) told me he was consolidating his business with Jameson, which would make it a larger business." [Tr. p. 87.]

Before entering into the contracts herein above mentioned, Mr. Pauley investigated Mr. Meyers' financial condition. [Tr. p. 87.] He testified as follows:

> "As to his financial standing at that time, I knew just what I investigated at the time I entered into the contract. I made some investigations. I made an inquiry from the Standard Oil Company, who he gave me as reference. I first discussed the matter with Mr. Melcher, the assistant district sales manager, and later over long distance telephone with Mr. Quinn of San Francisco, the general sales manager, both of the Standard Oil Company. I told Mr. Melcher that we were about to enter into a contract with Robert F. Meyers and would have to extend him some credit, and asked him to advise me what the record had been with him, as they had been selling him for a number of years. He told me he would have to check it up with the credit department and would call me back over the phone. In the course of the day he called me back and he said their records

showed they had extended Mr. Meyers credit up to $10,000, which had been quite satisfactory, with the authority of this office; that the records further showed with the authority of the San Francisco office, which was the head office, that they had at times extended him a credit of $25,000 and that their records showed it was reasonably satisfactory. Then later I asked him who in the San Francisco office had authorized that and he told me Mr. Quinn, general sales manager, who was the former district manager in Los Angeles, was quite familiar with it, so I called Mr. Quinn over the long distance telephone and his statements corroborated those made by me to Mr. Melcher in the local office. On that basis I authorized our office to extend this credit." [Tr. pp. 81-82.]

A "couple of weeks" after the written contract was signed, Mr. Meyers told Mr. Pauley he had ten or eleven service stations. [Tr. p. 108.] While Mr. Pauley testified that Mr. Meyers had told him many times, both before and after August 13, 1925, that he (Mr. Meyers) owned the Triangle Service Stations, Mr. Meyers denied this, and we shall therefore assume that Mr. Meyers did not make such statements; nevertheless Mr. Pauley's testimony that he at all times prior to February, 1926, believed Mr. Meyers owned these stations and that these stations were "merged into the firm of Jameson & Meyers" [Tr. p. 94] is not only uncontradicted but his belief, even if Mr. Meyers did not make the statements, was not unwarranted. The business conducted at these service stations was the same as that in which both of the bankrupts had been and were then engaged. As already pointed out, in 1923, Mr. Pauley negotiated with Mr. Mey-

ers for the sale of gasoline for the Triangle Service Stations. The bankrupts had their office at one of these stations and Mr. Meyers was seen there in connection with the transactions here involved several times by Mr. Pauley and on numerous occasions by Mr. Sohus. It was there that Mr. Sohus received most of the payments here involved. [Tr. p. 96.] Mr. Pauley and Mr. Sohus testified that these stations were by large signs designated, "Triangle Service Station, *R.* Meyers, Sole Owner," that they believed "R." stood for Robert," and that they did not know of Rosabelle Meyers until about February 2, 1926, when appellant, in a civil action, attached these service stations. They testified that immediately after the attachment Mrs. Meyers made a third-party claim, claiming these service stations as her property, and that "R. Meyers, Sole Owner" was changed to "Rosabelle Meyers, Sole Owner." [Pauley: Tr. pp. 93, 112; Sohus: Tr. pp. 97-98.] While Mr. Meyers did not deny the attachment and third-party claim, he did deny that these stations ever were designated "R. Meyers, Sole Owner." [Tr. p. 106.] It should be noted, however, that neither A. P. McCullough (in the transcript some times spelled "McMullough"), one of Mrs. Meyers' alleged office employees, or Joseph M. Devere, an office employee of the bankrupts, both called as witnesses by appellee, denied the testimony of Messrs. Pauley and Sohus.

So far as this controversy is concerned, only two provisions of the written contract are material. The first relates to suspension of deliveries and so far as material here, reads as follows:

> "First party shall not be required to make deliveries unto the second party at the times and in the

manner herein provided in the event that it is unable to do so by reason of . . . . inability to purchase crude oil at the prevailing market posted price in the open market." [Tr. p. 119.]

The second provision relates to terms of credit and reads as follows:

". . . . On the first of each month payment will be made for all deliveries up to and including the 15th day of the preceding month, and on the 15th of each month payment will be made for all deliveries up to and including the last day of the preceding month, with the exception that in case the party of the second part may sell to large commercial accounts, then in such cases the party of the first part will extend such credit to the party of the second part equivalent to the credit extended by the party of the second part to such commercial account." [Tr. pp. 121-122.]

If the referee's finding [Referee's Original Findings, Tr. p. 23] that "said account with the bankrupt was a thirty (30) day account and said contract between said parties provided for a settlement of said account monthly" means anything other than the plain import of the above quotation, then it is not supported by the evidence, and the 6th assignment of error [Tr. pp. 129-130] is justified.

Under the oral contract deliveries of fuel oil were to continue until ordered stopped by the Gas Company. [Tr. p. 81.] Shipments of fuel oil were made to and including August 31, 1925, at which time the Gas Company notified appellant that it wanted no more. [Tr. pp. 81, 88.] In regard to the terms of payment Mr. Pauley testified as follows:

"On the fuel oil contract the first agreement as to the date of payment was that we should bill direct to the Los Angeles Gas & Electric Corporation and should collect from them and to allow Mr. Meyers a brokerage for making the sale. Later on, before the deliveries actually started, he requested we make the shipment direct and the bill of lading to the Los Angeles Gas & Electric Corporation but to render the invoice to him, that he would collect for them on their regular pay day, which was the 20th or 21st of the month following in which the deliveries were made. If I remember correctly the last delivery of fuel oil was made on the last day of August, 1925. I did not have any conversation with Mr. Meyers about that time as to when payments would be made for that fuel account. Previously he stated it would be made on the 20th of the following month, which would be the 20th of September." [Tr. pp. 82-83.]

Nothing of any consequence occurred until September 20, 1925. At that time the amount due on the fuel oil account was $14,481.65. When appellant requested payment, Mr. Meyers stated that some of the shipments of fuel oil had not arrived at the Gas Company's side tracks until in September, that it was said corporation's policy not to make payment until the 20th of the month following the month in which the shipments were completed, and that consequently he had not received payment from the Gas Company and therefore could not pay appellant. [Tr. pp. 83, 88.] Concerning the Gas Company's practice in regard to payment in such cases, Mr. Pauley testified:

"I don't know whether that practice had been followed previously. We had not shipped them previ-

ously. We shipped to them just during the month of August. We had never done business with them before." [Tr. p. 88.]

When Mr. Meyers advised appellant that he could not then pay the fuel oil account, Mr. Pauley and Mr. Sohus asked Mr. Meyers to give appellant a trade acceptance for the amount. This he agreed to do, and on the following day Exhibit D [Tr. p. 125] was executed, accepted and delivered. [Tr. pp. 83, 95.] The due date on this trade acceptance was October 21, 1925. [Tr. p. 125.] The reason for requesting the trade acceptance was that appellant was "a small concern—handling a large volume of business and could not tie up (its) money in long term accounts; had to turn over (its) money" [Tr. p. 105], and that it would be able to obtain credit on a trade acceptance at its bank. [Tr. pp. 83, 101.]

At the time this trade acceptance was executed, nothing was due on the gasoline account. [Tr. pp. 90-91.] Mr. Pauley's testimony is the only evidence upon this subject in the entire record, and it completely disposes of the referee's finding that there was then due approximately $9,000 [Referee's Original Findings, Tr. p. 22], assigned as error [1st Assignment of Error, Tr. p. 128]. The referee failed to consider the terms of the contract extending credit to the bankrupts. He did not distinguish, and later only reluctantly admitted the distinction, between an account payable but not due and a due or past due account.

Appellant continued to sell and deliver gasoline to the bankrupts, and nothing of any consequence happened until October 3, 1925, when appellant notified Mr. Meyers

by letter that it could no longer purchase crude oil at the prevailing market posted price in the open market and that pursuant to the provision of the gasoline contract relating to suspension of deliveries (hereinabove quoted) it would suspend further deliveries of gasoline "upon the 8th day of October, 1925, and until such date thereafter as said Pauley Oil Company shall be able to purchase crude oil at said prevailing market posted price in the open market," etc. [Tr. pp. 123-124.] Mr. Pauley testified that the contract was suspended for no reason other than the one stated in the notice of suspension. [Tr. pp. 80, 86.] Mr. Meyers, however, said the reason for the suspension was that "Pauley could not buy in the open field; his credit was shot." [Tr. p. 71.] *Whatever the reason for the suspension of deliveries, clearly it was not that appellant had lost any faith in the bankrupt's financial condition.* At this time the trade acceptance had not matured and, according to Mr. Sohus, the bankrupts had kept the gasoline account in a good condition although they had not made all their payments "just exactly according to the contract." On that date there was only $3,224.36 due on this account and that amount was then only three days past due. [Tr. p. 99.] Mr. Sohus' testimony is the only evidence in the entire record showing the amount then due, and it belies the finding that there was then due "approximately $23,000.00" [Referee's Original Findings, Tr. p. 22], which finding was assigned as error [4th Assignment of Error, Tr. p. 129]. In attempting to justify this finding, the referee said:

> "The use of the word 'due' in the opinion, in accordance with the commercial vernacular, might have been technically incorrect, and 'unpaid' would have

been a better and more appropriate term." [Tr. p. 56.]

Concerning a similar finding he said:

> "As in another instance previously referred to, it may be that, adopting the vernacular of credit men, a more appropriate term would have been 'unpaid' instead of 'due.' [Tr. p. 65.]

The fact is, we are dealing with credit and "credit men," and in cases such as this there is a tremendous difference between an account payable but not due and an overdue account. Merchants are little concerned with the amount of accounts receivable on their books, but they are concerned with accounts past due.

Furthermore, the evidence not only belies the referee's finding that appellant "terminated" the contract [Tr. p. 24]; assigned as error, [Tr. p. 131], but also the statement in his opinion that, "Its business relations with the bankrupt were terminated and there was no necessity for preserving its goodwill and the claimant had no further interest in the bankrupt except to secure payment of its account." [Tr. p. 49.]

The next event of importance occurred on or immediately after October 21, 1925, the due date of the trade acceptance. Mr. Meyers failed to honor the trade acceptance. It appears that when appellant completed its deliveries of fuel oil, the bankrupts purchased fuel oil from the Standard Oil Company and used the payments received from the Gas Company for the fuel oil delivered by appellant to pay the Standard Oil Company. [Tr. p. 73.] Mr. Pauley's testimony relates what occurred next:

"About the next day after this trade acceptance came back to us I had a conversation with Mr. Meyers as to payment of the trade acceptance. Mr. Sohus was present. We asked him why he had not paid the trade acceptance, and he said it was due to the absence of Mr. Stewart of the Farmers & Merchants National Bank, with whom he and Mrs. Meyers had always done their business; that Mr. Stewart was absent and he could not make arrangements for funds until he returned. We asked him what he did with the money that he received for this fuel oil and he evaded an answer, to the best of my recollection, as to what he did with the money." [Tr. pp. 83-84.]

On cross-examination Mr. Pauley amplified the foregoing testimony as follows:

"When that was due and not paid, that is the time that he stated he was getting the money from the Farmers & Merchants National Bank and that Mr. Stewart was away. He said Mr. Stewart would return in 10 days, if I remember correctly, some time about that. We asked him why he had not paid the trade acceptance at the bank when it was presented and he said he went to the bank to secure the funds and found that Mr. Stewart was away, was in New York, and that he had only dealt with Mr. Stewart, and that as soon as he returned he would borrow the money from him. The next move we made in that matter, if I remember correctly, we waited until Mr. Stewart returned. I don't recall when that was. I had a conversation with Mr. Meyers after Mr. Stewart returned. I don't recall the date of that conversation, and I am only reciting the dates there by the exhibits, but as soon as he returned we had a conversation with Mr. Meyers. It was some time in October. We had called up the bank

and found out that Mr. Stewart had returned, and then we went up to see Mr. Meyers and told him we understood Mr. Stewart had returned and asked him if he had secured the money and he said he was sorry, that he was unable to do it, that he had a talk with Mr. Stewart and was unable to borrow any more money. The only other conversation was about the payment of the account, as to how he would pay it. He said that he would pay the trade acceptance just as fast as he could get the money from his various business. I don't recall of having any more conversation with him personally. The rest of it was handled by Mr. Sohus, I think." [Tr. pp. 89-90.]

While Mr. Meyers denied making similar representations *to Mr. Sohus* [Tr. p. 76], he did not deny making such representations to Mr. Pauley, or otherwise contradict Mr. Pauley's testimony although he was called in rebuttal after Mr. Pauley's testimony had been given. Evidently in this respect the referee believed Mr. Pauley. [Referee's Opinion, Tr. p. 46.]

Mr. Meyers told Mr. Pauley "he would pay the trade acceptance just as fast as he could get the money from his various business." [Tr. p. 90.] Almost immediately thereafter he began making substantial payments. The dates and amounts of these payments are:

October 27, 1925	$ 500.00
October 31, 1925	500.00
November 5, 1925	500.00
November 11, 1925	500.00
November 16, 1925	1500.00
November 23, 1925	500.00
November 25, 1925	2500.00

December 3, 1925	2500.00
December 14, 1925	2000.00
December 21, 1925	500.00
December 26, 1925	1500.00

The foregoing payments, totaling $13,000, were all received within four months of bankruptcy and by appellant applied upon the trade acceptance. [Tr. p. 105.] The referee found that to the extent of $9100 they constituted a voidable preference.

The fact that said payments were made with consistent regularity and, on the whole, in increasing amounts, taken in conjunction with knowledge that the bankrupts' business had apparently not diminished and that they were able to buy gasoline from other companies on credit, would assure a reasonable person that the bankrupts were solvent.

As to the volume of business apparently done by the bankrupts after October 3, Mr. Sohus testified:

> "During all this time Jameson & Meyers continued to operate. I did not notice any difference in the extent of their operations. I did not notice any difference between October 3, 1925, and December 26, 1925, any difference in the extent of their operations. As far as I knew they were operating as extensively, that is, selling, or handling as much gasoline and oil on the 26th of December, 1925, as they were on the 3rd day of October, 1925." [Tr. p. 100.]

Concerning credit extensions by other dealers to the bankrupts, Mr. Pauley testified as follows:

> "Immediately after we ceased delivering gasoline and fuel oil to Mr. Meyers we learned that Mr. Meyers was able to buy gasoline from other sources. We

learned that he was buying oil or gasoline from the Seaboard Petroleum Corporation and from the Shell Oil Company. The Seaboard Petroleum Corporation advised me they were delivering him on credit, and I learned through Mr. Sohus that the Shell Oil Company's credit manager, Mr. Dahl, told him they were delivering him on credit. These companies were delivering the day we ran the attachment because through a misunderstanding we attached one of their trucks. That was in February, 1926, and up to that time I did not know whether or not either of these two companies, the Seaboard or Shell, had cut off credit, denied further credit to Mr. Meyers. The sales manager of the Shell Oil Company advised me the day previous to our running the attachment that they were extending him credit." [Tr. pp. 84-85.]

Upon the same subject Mr. Sohus testified as follows:

"I know of my own knowledge that Mr. Meyers had obtained extensions of credit from other dealers in gasoline after the 3rd day of October, 1926. In conversation with Mr. Dahl, credit manager of the Shell Oil Company, about November, I would say, the latter part of November, I was just talking with him as we did quite often, talking back and forth regarding various things, and I asked him if he was extending Meyers credit. In the first place, he had called me to find out our experience with him at the time they took on the account. That was possibly a week or 10 days after October 3rd. I told him how much he owed us, how much was due, and how much was past due. This second conversation that I had with Mr. Dahl in regard to Mr. Meyers' financial standing or the financial standing of Jameson & Meyers was just during the course of another conversation. He called me regarding another customer and I incidentally asked him about it and he

said they were extending him credit but he didn't ask for details of it. I knew the Seaboard Petroleum Corporation was extending credit to Mr. Meyers but I did not know how much credit they were extending. I couldn't state positive when I learned that but I think it was about possibly in November." [Tr. pp. 99-100.]

While there is evidence that while the payments in question were being made to appellant the bankrupts made no payments to any other creditors [Tr. p. 69], *there is absolutely no intimation in the record that appellant was aware of that fact, if it is a fact.*

Concerning further investigation of Mr. Meyers' financial condition, Mr. Pauley testified, as follows:

"When we were having difficulty in collecting our trade acceptance in full, I went back to the Standard Oil Company who had recommended Mr. Meyers. I went to San Francisco, made a special trip to discuss it with Mr. Quinn, some time in the early part of November, 1925. I told Mr. Quinn about Meyers owing us this money, that I had extended him credit based upon his recommendation, and that it had not been paid and that I wanted his advice regarding it. His reply was that Meyers had always paid their account and that I should insist upon him paying this immediately and at once. When I came back we insisted upon having the account paid and we continued to insist until the date we had the attachment suit filed. I did inquire about the Triangle Service Stations on that trip, and Mr. Quinn said that in his opinion Robert F. Meyers was worth $250,000 and should be able to pay this account promptly. He did not tell me that the Triangle Service Stations was the separate property of Mrs.

> Meyers. I came back and insisted immediately on the payment of our money and was not successful in getting it. I reported that to Mr. Quinn the next time I saw him. I did not make a special trip to see him. I told him Meyers seemed pretty badly tied up. I don't recall when that was. He said that he was surprised. This was possibly 60 or 90 days after this November trip. I couldn't say. It may have been after the filing of the attachment suit." [Tr. pp. 94-95.]

That appellant was extremely anxious to get its money as soon as possible is admitted. It was a small concern and needed its money in its business. [Tr. p. 111.] We may also concede—for Mr. Meyers so testified—that Mr. Sohus was told that some of the eleven payments were made by checks drawn on the Triangle Service Stations account (Mrs. Meyers' account), and that Mr. Sohus told Mr. Meyers that "he didn't give a damn where it (the money) came from." [Tr. p. 70.] Mr. Sohus testified that in seeking to collect this money he was not prompted by "any idea of insecurity of the account, but because of our own necessity for money." [Tr. p. 106.]

Mr. Pauley testified that—

> "I did not know of my own knowledge the amount of assets, that is, the reasonable value of the assets or the liabilities of Jameson & Meyers or Mr. Meyers from the time we ceased delivering gasoline to the time we received the last payment. I believed they were solvent all the time, and as to Mr. Meyers I still believe it." [Tr. p. 85.] * * *
>
> "I believed at all times that Mr. Meyers was solvent. I believed that at the time of the filing of the petition in bankruptcy. Pauley Oil Company had

something to do with the application for the appointment of a receiver. I did not handle it personally. I did not sign the petition that I recall. I don't recall whether it was ever referred to me for my approval. I still believe he was solvent, notwithstanding the filing of the petition. In other words, I believe this business in his wife's name belongs to him. I didn't know anything about his wife owning the Triangle Service Stations until it came out in the bankruptcy." [Tr. pp. 92-93.]

Mr. Sohus testified:

"At the time these payments were made, commencing with October 27th, the first payment of $500, and ending with December 26, with a payment of $1500, I did not know whether or not Jameson & Meyers or Mr. Robert F. Meyers were insolvent. I considered them solvent. That was my belief." [Tr. p. 99.] * * *

"During this time I did not know the reasonable value of the assets of Jameson & Meyers as compared with the liabilities." [Tr. p. 100.]

We have now detailed all of the events and circumstances disclosed by the record which occurred during the period of time that the payments constituting the alleged voidable preference were received, and it is upon that record as thus set forth, we respectfully submit, that the issues involved in this appeal must be determined. The record contains evidence of alleged conversations between Mr. Meyers on the one hand, and Mr. Pauley and Mr. Sohus on the other,—conversations disclosed primarily by the testimony of Mr. Meyers. To this evidence we shall now call attention, and in each instance we shall point out by the record itself that the alleged conversa-

tion occurred after the last payment was received. Either because of Mr. Meyers' belligerent attitude and apparent lack of frankness and candor or because of an unusually forgetful mind and memory a careful scrutiny of his evidence is required.

Before proceeding to a consideration of his evidence concerning these conversations, we feel constrained to paint this man's remarkable mind and memory. He testified:

> "Our credit at the Pauley Oil Company had been stopped prior to October 27, 1925,—I should judge 2 or 3 or 4 months prior, I am not sure." [Tr. p. 69.]

The fact is that the bankrupts had never had any dealings with appellant prior to August 13, 1925, that fuel oil was sold to them on credit up to August 31, 1925, when appellant was ordered by the Gas Company to stop further deliveries, and that sales and deliveries of gasoline continued under the same terms of credit until October 7, when they were suspended for reasons other than the bankrupts' financial condition.

When Mr. Meyers was asked to identify Exhibit B, the notice of suspension of gasoline deliveries addressed to him, he could not remember that he had ever, and he was almost positive that he had never, received or seen such a letter or taken it to his attorneys. [Tr. pp. 71, 72.] Yet he unhesitatingly identified a letter [Exhibit C, Tr. pp. 124-125] written at his instance by his attorneys Lawler & Degnan, to appellant clearly in reply to Exhibit B. [Tr. p. 72.]

He could not recall when he received the last consignment of gasoline from appellant, and, as to the amount of fuel oil he agreed to buy, he testified as follows:

> "I don't remember how many gallons of fuel oil I agreed to buy. I bought so many tank cars, I think, but I don't remember how many. Very few; maybe 4 or 5, something like that, were delivered to the Los Angeles Gas & Electric Corporation." [Tr. p. 72.]

Asked how many conversations he had with Mr. Pauley, he testified:

> "I think I had one conversation with Mr. E. L. Pauley, I don't remember when it was. He was down in his office or something. It wasn't at the time that the gasoline contract was signed. I did not see Mr. Pauley in connection with that contract. As far as I recall now I saw Mr. Pauley on only one occasion. The subject of that conversation was that he was not looking to Jameson for any of his money; he was looking to me for it. I don't remember the date of that conversation; it was at his office somewhere over there on the stock yards. No one present except Mr. Pauley and myself." [Tr. pp. 72-73.]

When called on rebuttal he remembered a second conversation [Tr. p. 107], and then, apparently unwittingly, he gave testimony of a third conversation [Tr. p. 108]. The referee found that he had had still another conversation with Mr. Pauley. [Tr. p. 23.]

Concerning the proceeds of the fuel oil purchased from appellant and delivered to the Gas Company, Mr. Meyers first testified:

> "I made an assignment of that account to the Farmers & Merchants National Bank for the oil

> I bought from the Standard Oil Company." [Tr. p 73.]

Later he testified squarely to the contrary, thus:

> "That money that I assigned in that fashion was not the proceeds of this fuel oil which I had purchased from the Pauley Oil Company; that was Standard Oil Company business, their own oil. They are not taking anybody else's money." [Tr. p. 110];

and he further testified that he had assigned the money due him from the Gas Company to Standard Oil Company "6 or 7 months before the bankruptcy proceedings" [Tr. p. 110], a time when neither the account nor his dealings with Standard Oil Company in regard to fuel oil existed in fact or in the contemplation of any of the parties.

He testified that after appellant suspended deliveries of gasoline he bought from the Shell Oil Company and that,—

> "I paid cash to the Shell Oil Company when I started, but I don't know how long I continued to pay cash. Thereafter I bought on credit, on time." [Tr. p. 75.]

Later he reversed himself entirely, saying that at first and for only a few days, he was able to buy on credit and thereafter he had to pay in actual cash, "they would not even take a check." [Tr. p. 108.]

Although he purchased on credit at least $30,000 worth of gasoline from the Shell Oil Company, he didn't know the dates when that obligation was incurred. [Tr. p. 109.]

Other instances of Mr. Meyers' faulty memory will be disclosed in the quotations of his evidence concerning the alleged conversations.

In addition to the events already fixed as to time, the period in which the conversations to be referred to occurred can be fixed by reference to the time of a meeting of the bankrupts' creditors, referred to as the "creditors' meeting," held in the office of the Standard Oil Company. Mr. Meyers fixed the time of the meeting as "maybe 4 or 6 weeks before (he) was put into bankruptcy" [Tr. pp. 74-75], in other words, between the 2nd and 16th of January, 1926. Mr. Sohus testified that this meeting occurred "about two weeks before we ran the attachment" [Tr. p. 98]; and that the attachment "was run" February 2, 1926, [Tr. p. 78]. It appears that at this meeting at least some of the creditors agreed to give the bankrupts a six months' moratorium. [Tr. p. 75.]

We shall now set out the conversations as they appear in the record. Mr. Meyers testified:

> "Every morning I would go there (his office in one of the Triangle Service Station buildings) I would find Mr. Sohus waiting there. There was a conversation every time he was there. I told him we were in trouble, and he knew we were in trouble. *He had attended a meeting before that* (the creditors' meeting) and had agreed to give me 6 months time to get the firm out of bankruptcy, and I said, 'On top of that you are saying here every morning and telling me you don't care where I get it or what the condition of the business is as long as you get yours.'" [Tr. pp. 68-69.]

Obviously this conversation occurred after the last payment was received by appellant.

Mr. Meyers also stated that *some time after* October 27, 1925, he asked appellant "for credit," but, although asked to fix the time, the witness either could not or would not do so. [Tr. p. 69.]

He next referred to a conversation with Mr. Sohus and an attorney had at his office some time after the creditors' meeting, but nothing in this conversation refers to any time prior to the creditors' meeting. [Tr. p. 70.] The occurrence, however, is of considerable importance in this, that it was after this conversation that Mr. Sohus first threatened to resort to bankruptcy proceedings. (See next paragraph below.)

Again Mr. Meyers testified:

> "Mr. Sohus threatened every time he came into the office *with his white automobile. The first time this occurred was when the money stopped coming regularly to him. That was for several weeks that he came there, I can't remember the dates.* If I gave him $500, he wanted a thousand if I gave him $1,000, he wanted $1500; if I gave him $1500, he wanted $2,000; anything I gave him he was not satisfied with. I kept at Mr. Sohus for months for Mr. Pauley to come up as we could have gotten along together. He threatened to throw us into bankruptcy a dozen times ever since he came there to us *and could not get his money. I couldn't give you the dates. I have no reason to carry them in my mind and I could not give them to you. He threatened it the first time when he was there with the lawyer and did it right along after, all along. That was at 17th and Hope, at Jameson & Meyers office.*

That conversation did not take place in January of 1926. I don't know the name of the lawyer. *I had only one conversation with Mr. Sohus in which an attorney was present.* I never talked to Mr. Pauley except in his own office and no attorney was present.

"*I don't remember I gave any special dates concerning my conversations with Mr. Sohus.* All I know is he kept on pushing us and telling me he wanted the money, and he didn't care where it came from or anything else, kept on. He was at a special meeting in the Standard Oil Company's office, a creditors' meeting, when I stated that if I were given a little time I thought I would be able to work things out. I don't know who was present at that creditors' meeting. Mr. Sohus ought to know. I will say Mr. Sohus was present; he agreed to give me time and did not hardly wait to get out before he started riding me. That meeting was in the credit department of the Standard Oil. Somebody from the Shell, and the credit man of the Standard Oil Company, and Mr. Sohus, and I think Mr. Weitzel of the Sierra were present. *That was maybe 4 or 5 weeks before I was put into bankruptcy.*" [Tr. pp. 73-75.]

Referring to the above quotation, the evidence does not show when Mr. Sohus "came into the office with his white automobile." In the second place, "the money stopped coming in regularly to him" *after December 25, 1925.* What Mr. Meyers meant by the phrases, "when the money stopped coming regularly to him," and, "ever since he came there to us and could not get his money," is clearly explained by his own evidence. He fixed the time when Mr. Sohus first threatened bankruptcy proceedings in two ways: one, it was after the money stopped coming regularly to Mr. Sohus, and two, it was after the

occasion when Mr. Sohus, with a lawyer, called at Jameson & Meyers' office. As we have already pointed out, the latter event occurred after the creditors' meeting. [See Tr. p. 70.] Consequently, Mr. Meyers must have meant by the above quoted phrases that the money stopped coming reguarly to Mr. Sohus after the creditors' meeting, *i. e.*, after the last payment was received by appellant, after December 26, 1925. Beyond this, Mr. Meyers couldn't give any dates and in effect disclaimed giving "any special dates" concerning his conversation with Mr. Sohus. The whole tenor of the quoted evidence points unerringly to the conclusion that all the events narrated occurred after the last payment was received. Yet a portion of this and the evidence contained in the preceding quotation from the transcript is relied upon by the referee [Tr. pp. 57-62] to sustain the finding "that during said period, by continual pressure and threats, claimant endeavored to secure all possible funds before the crash of the bankrupt company" [Tr. p. 24], but he omitted all reference to Mr. Meyers' statement that Mr. Sohus threatened bankruptcy "the first time when he was there with the lawyer," and also Mr. Meyers' own confession that he couldn't give any dates. [Referee's Certificate, etc., Tr. p. 60.]

Mr. Meyers testified that Mr. Sohus asked him to get a note from Mrs. Meyers guaranteeing his indebtedness to Mr. Pauley and he would keep it until after the bankruptcy proceedings were over. He said: *"This specific conversation was shortly after that meeting in the Standard Oil Company* (the creditors' meeting)." [Tr. p. 77.]

Finally, Mr. Meyers related a conversation with Mr. Pauley that occurred at the "Independent Petroleum Re-

finers' (Marketers') Association, or something of that kind." He testified:

> "I had a conversation with Mr. Pauley where the matter of my solvency or insolvency was discussed That was a conversation that I forgot about yesterday. It was after that trade acceptance was given to him and after it came back; right after it came back. The conversation took place at the Independent Petroleum Refiners Association, or something of that kind, and we met Mr. Tapper and Mr. McCullough, and I met Mr. Pauley up there. Mr. Pauley and somebody that represented that association—I don't remember his name,—were present. Mr. Pauley was excited, said, 'You ought not to have given this trade acceptance unless you thought you were going to take care of it,' and I told him that I gave him the trade acceptance because Mr. Sohus asked for it and wanted to use it to get money, and that Mr. Sohus at that time did not think I would be able to take care of it because he knew we were pushed all around to get by, and the man that was there at the time said, 'There is no use arguing with these fellows. These fellows were broke and you knew they were broke at the time. Why didn't you stall along with them?' Almost ended in a murder or something on the top floor going to kill someone." [Tr. p. 107.]

The meeting above referred to was undoubtedly held after the last of the payments here involved was received by appellant and shortly after the creditors' meeting was held. Mr. Pauley fixed the time of this meeting as "about or shortly after the middle of January, 1926." [Tr. pp. 112-113.] Mr. Sohus fixed the same time. [Tr. pp. 113-114.] Mr. McCullough, who was present, couldn't

fix the time at all. [Tr. p. 112.] Mr. Meyers testified that the meeting occurred "right after (the trade acceptance) came back." The words "right after" are most indefinite, but Mr. Meyers, apparently unwittingly, gave us a much more definite clew to the time of this meeting when he testified: "* * * the man that was there at the time said, * * * *'Why didn't you stall along with them?'* " This testimony can only refer to the agreement of the creditors to give Mr. Meyers "6 or 7 months' time without calling on (him) to pay them anything, to give (him) a chance to get things together." That agreement was reached at the creditors' meeting [Tr. pp. 74-75], *and that was the only time that the matter of "stalling along" with the bankrupts was ever considered.* [Tr. pp. 68, 70, 74-75.] Consequently the conversation related by Mr. Meyers must have taken place *after* the creditors' meeting,—after the last payment was received. And although what Mr. Sohus thought and knew was a pure conclusion of the witness, and therefore incompetent, this evidence is discredited by the potent fact that up to October 3 the bankrupts kept the gasoline account, an account much larger than the trade acceptance, in satisfactory condition, and by the further fact that at the time the trade acceptance was given all parties understood that the proceeds of the fuel oil sold by appellant to the bankrupts and by the latter to the Gas Company would be available to the bankrupts and applied by them to the payment of the trade acceptance. What "the man that was there" said is purely hearsay and therefore incompetent as evidence. The belligerent character of this witness, which, not only characterized but warped his entire testimony, is demonstrated by the last sentence,

"Almost ended in a murder or something on the top floor going to kill someone." Furthermore, we respectfully submit that because of the discursive, rambling character of all of his testimony, his general inability or unwillingness to fix dates as to other and at least equally important matters, and the frequent contradictions in his testimony, coupled with the fact that this was one of the several conversations that he "forgot about" when he was first called as a witness, no conclusion adverse to appellant should be drawn from his testimony as to the time of this meeting. The burden of proof was upon the trustee, and if it was his contention that this meeting took place prior to the receipt of the last payment, he should have definitely fixed the time.

Mr. Pauley testified that he had had "no conversation prior to the receipt of the last payment from Mr. Meyers on or about December 26, in which insolvency or bankruptcy of Mr. Meyers, or Jameson & Meyers, was mentioned." [Tr. p. 85.] Mr. Sohus testified that he never mentioned or threatened bankruptcy prior to the creditors' meeting. [Tr. pp. 97, 98.] In this, as we have already pointed out, he was corroborated by Mr. Meyers.

We have now carefully, exhaustively, and, we believe, fairly reviewed all the evidence. The referee, however, made certain findings that are not supported by any evidence. For instance, the finding "That it is true that * * * aside from the Los Angeles Gas & Electric Corporation purchases of crude (fuel) oil, the sales of the bankrupt co-partnership were on a cash basis." [Tr. p. 24; assigned as error, Tr. pp. 130-131.] The referee admits that no such evidence was introduced and says he merely drew such a conclusion. [Tr. p. 62.]

The referee further found that appellant's total "claim" (meaning evidently the total value of gasoline and fuel oil sold to bankrupts) was "in excess of" $75.000. [Tr. p. 23.] He confesses that "It does not appear from what source this statement of evidence was taken to be included in the findings and it is immaterial to the decision and not properly a part of the findings." [Tr. p. 57.] So far as the evidence shows, the total value of the gasoline and fuel oil sold is $61,135.47. [Tr. pp. 9-10] while the actual amount in fact is $62,166.83.

IV. Summary of Facts.

We feel that the length of our review of the evidence not only justifies but requires a brief summary of the facts.

Appellant was a small company, operating on limited capital, and could not afford to have its money tied up in long term accounts. The bankrupts had each for himself been engaged in the service station business for a number of years. Mr. Pauley had known Mr. Meyers for about five years prior to August 13, 1925. He knew that Mr. Meyers owned and operated a number of service stations. He knew very little of Mr. Jameson other than that he had been and was engaged in the retail gasoline business. However, Mr. Meyers told him that "he was consolidating his business with Jameston, which would make it a larger business."

Before executing the gasoline contract, Mr. Pauley investigated Mr. Meyers' financial standing and ascertained that he enjoyed an open credit with the Standard Oil Company to the extent of $25,000. Thereupon the gasoline and fuel oil contracts were executed. Shortly after the

execution of these contracts Mr. Meyers told Mr. Pauley that he had ten or eleven service stations. Mr. Pauley and Mr. Sohus believed, and not without good cause, that Mr. Meyers owned the Triangle Service Stations, and that these stations were merged into the partnership assets.

Deliveries of gasoline were made regularly from August 13 to and including October 7, 1925. On October 3 appellant notified Mr. Meyers that deliveries under the contract would be suspended from and after October 8 and until it could again buy crude oil on the open market at the prevailing market posted price, but the contract was not terminated. The contract required payments for gasoline deliveries to be made every fifteen days. Up to October 3 this account was kept in a satisfactory condition. On October 3 there was only $3,224.36 due,—this sum was then three days past due.

Deliveries under the fuel oil contract were made from August 14 to August 31, when further deliveries were ordered stopped. When this contract was executed Mr. Meyers stated that payment would be made on the 20th of the month following deliveries. On September 20 he explained that some of the fuel oil was not received by the Gas Company until September and that it was said corporation's custom not to make payment until the 20th of the month in which the order was completed,—in this case, October 20. Mr. Pauley did not know said corporation's custom—he had had no previous dealings with it,—but he apparently accepted the explanation, and in lieu of cash took the trade acceptance. At this time nothing was due on the gasoline account.

The trade acceptance fell due on October 21, at which time Mr. Meyers failed to honor it. In the meantime he had assigned the proceeds of the fuel oil account to the Standard Oil Company and when Mr. Pauley asked him what he had done with this money, he evaded a direct answer. He did state, however, that he had expected to get the money from the Farmers & Merchants National Bank but due to the absence of Mr. Stewart, an officer with whom he and Mrs. Meyers had always dealt, he had not yet succeeded. Later, and after Mr. Stewart's return, he told Mr. Pauley that the bank would not lend him any more money, but that he would pay the account as fast as he could get his money from his various businesses. Thereupon and from October 27 to and including December 26, 1925, he made eleven payments ranging from $500 to $2500 in amount and totaling $13,000. These payments were by appellant applied upon the trade acceptance. Most of these payments were made in the bankrupt's office in one of the buildings of the Triangle Service Stations, where Mr. Sohus called for them. Appellant was extremely anxious to get its money as soon as possible, for it needed it in its business.

When the bankrupts failed to pay their entire indebtedness promptly, Mr. Pauley in November discussed the matter with Mr. Quinn of the Standard Oil Company who had previously recommended Mr. Meyers as a good financial risk. Mr. Quinn reassured Mr. Pauley,—he said Mr. Meyers had always paid his accounts with the Standard Oil Company and that he considered him worth $250,000.

While the payments were being made the bankrupts seemed to be doing as large a business as during the time

appellant was delivering gasoline to them, and appellant learned that they were buying gasoline on credit from the Shell Oil Company and the Seaboard Petroleum Corporation. Shell Oil Company is now a creditor of the bankrupts in the sum of $30,000, and while it does not so appear in direct language, it is fairly inferable from the record [Tr. p. 75] that said indebtedness grew out of the sale of gasoline on credit after appellant suspended deliveries. Neither Mr. Pauley nor Mr. Sohus knew the amount of the bankrupts' assets or liabilities but both believed them solvent. Mr. Pauley added that he still believes that Mr. Meyers is solvent, stating that he believes that the Triangle Service Stations in fact belong to Mr. Meyers.

We respectfully submit that Mr. Meyers' own testimony demonstrates that the various conversations related by him all took place after the last payment was received and that therefore none of them is material or relevant to a consideration of the issues on this appeal. We maintain this view although the last conversation hereinabove set out does in part purport to refer back to the time when the trade acceptance was given. But as we have already pointed out, the references are in part mere conclusions of the witness and in part hearsay, and therefore the evidence thereof was incompetent and proves nothing. We also pointed out the obvious improbability of this evidence.

We believe we have fairly reviewed, appraised and summarized the evidence. If we have, it must be conceded that there is absolutely no support for the finding that appellant had actual knowledge that in receiving the payments a preference was being effected. The only

question remaining is: Did appellant have reasonable cause to believe that a preference was being effected? Stated in another form, the question is: Under all the circumstances disclosed by the record, do these facts, viz.: that after the suspension of deliveries of gasoline the bankrupts made no further payments to appellant until October 27, that the bankrupts failed to honor the trade acceptance when due, that when asked what he had done with the proceeds of the fuel oil sale Mr. Meyers made an evasive reply, that on or about October 21 Mr. Meyers could borrow no more money from his bank, and that in response to frequent demands the bankrupts made payments—eleven in number—on account of their indebtedness beginning with October 27 and ending with December 26 and ranging in amounts from $500 to $2500, support the finding that while receiving said payments appellant then had reasonable cause to believe that thereby a preference would be effected?

V. Argument.

1. The Provisions of the Bankruptcy Act.

Section 57g of the Bankruptcy Act provides:

> "The claims of creditors who have received preferences, voidable under section sixty, subdivision b, or to whom conveyances, transfers, assignments, or incumbrances, void or voidable under section sixty-seven, subdivision e, have been made or given, shall not be allowed unless such creditors shall surrender such preferences, conveyances, transfers, assignments or incumbrances."

Section 60a pertains to and defines the *giving* of a preference, while section 60b pertains to and defines the

receiving of a preference. We are concerned only with the latter section, for it is entirely immaterial to a decision in this case that the bankrupts may have *given* a preference to appellant within the meaning of the former section.

In re Carlisle, 199 Fed. 612, 616-617.

Section 60b reads as follows:

> "If a bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, *and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference*, it shall be voidable by the trustee and he may recover the property or its value from such person. And for the purpose of such recovery any court of bankruptcy, as hereinbefore defined, and any state court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

It has not heretofore been contended, and we do not believe that it will now be contended, that the payments in question were void or voidable under section 67e of the Bankruptcy Act. Such contention would find absolutely no foundation in the entire record; therefore we shall ignore it.

2. In Order That Appellant's Claim May Be Disallowed or Rejected, It Is Necessary That the Evidence Show Affirmatively That Appellant, or Its Agent Acting Therein, Then Knew or Had Reasonable Cause to Believe, That the Transfer Would Effect a Preference.

To establish a preference under section 60b four elements are necessary: (1) The transfer must be made from an insolvent person to a creditor; (2) the effect of such transfer must be to enable one creditor to obtain a greater percentage of his debt than others in the same class; (3) the creditor receiving it must have known or had reasonable cause to believe that the effect would be a preference; and, (4) the transfer must have been made within four months prior to the bankruptcy.

It is, of course, conceded that the payments in question were received within four months prior to bankruptcy. It is also conceded "that the bankrupts herein were insolvent at all times from and after the 27th day of October, 1925, and that during all of said time said bankrupts had other creditors of the same class as this claimant and appellant" [Tr. p. 114]. We are concerned, therefore, only with the third element of proof, viz.: the creditor receiving the transfer must have known or had reasonable cause to believe that the effect of the transfer would be a preference. The records must show affirmatively that this element was established by the evidence for the burden of proof was upon the trustee.

In *In re Shaw*, 7 Fed. (2d) 381, 382, the court said:

> "To constitute a preference under section 60a and 60b of this act (Comp. St. §9644), the following

four elements are necessary: ' "First, the transfer must be made from an insolvent person to a creditor; second, the effect of such transfer must be to enable one creditor to obtain a greater percentage of his or its debt than others in the same class; third, the creditor receiving it must have had reasonable cause to believe that the effect would be a preference; and fourth, the transfer must have been made within four months prior to the bankruptcy." ' Heyman v. Third Nat. Bank of Jersey City (D. C.), 216 F. 685, 686.

". . .

". . . The burden of proof on all the four mentioned elements is cast upon the trustee. Heyman v. Third Nat. Bank of Jersey City (D. C.), 216 F. 688, 689. See, also, Collier on Bankruptcy (13th Ed.), p. 1328, and cases cited under notes 302 and 303."

In *In re Pingel,* 288 Fed. 664, 666, the court, after quoting section 57g and 60b, said:

"It will be noted that two necessary elements of a voidable preference are (1) the insolvency of the bankrupt at the time of the making of the preferential transfer and (2) reasonable cause, on the part of the transferee, to believe that the enforcement of such transfer will effect a preference. If either one of these be lacking, the transfer in question is not a voidable preference under the Bankruptcy Act. . . .

"The burden of proving the facts necessary to constitute legal grounds for the asserted invalidity of the transaction involved rests upon the person asserting such invalidity. Whitney v. Dresser, 200 U. S. 532, 26 Sup. Ct. 316, 50 L. Ed. 584; Bank of Commerce

v. Brown, 249 Fed. 37, 161 C. C. A. 97 (C. C. A. 4); *In re Ann Arbor Machine Co., supra*" [278 Fed. 749].

In *Abdo et al. v. Townshend et al.,* 282 Fed. 476, 478, the court said:

> "To maintain such a suit [action to recover an alleged preference] it is necessary to show, and the burden of proof is on the plaintiff, that the bankrupt, (1) while insolvent, (2) within four months of the date of filing the petition in bankruptcy, (3) made a transfer of property; (4) that the transferee was thereby enabled to obtain a greater percentage of his debt than other creditors of the same class; and (5) that the person receiving the transfer then had reasonable cause to believe that the enforcement of such transfer would effect a preference."

In *In re K. G. Whitfield & Bro.,* 290 Fed. 596, 600, the court said:

> "In another view of this case, the claims of the contestants would have to fail. The law placed upon them the burden of showing that at the time of the transfer Whitfield & Bro. as a firm was insolvent, and that the American National Bank had reasonable cause to believe that the enforcement of the deed of trust made by the firm would enable it to obtain a preference. Tumlin v. Bryan, 165 Fed. 166, 91 C. C. A. 200, 21 L. R. A. (N. S.) 960; Barbour v. Priest, 103 U. S. 293, 26 L. Ed. 478; *In re* Klein (6 Cir.), 197 Fed. 241, 116 C. C. A. 603; Kimmerlee v. Farr, 189 Fed. 295, 111 C. C. A. 27; Turner v. Schaeffer, 249 Fed. 654, 161 C. C. A. 564, 40 Am. Bankr. Rep. 829. See, also, authorities cited to note 504, §614, p. 1249, Black on Bankrupcy (3d Ed.)."

3. Mere Suspicion Is Not Sufficient to Charge Creditors With Knowledge, or Reasonable Cause to Believe, That a Preference Will Be Effected.

In *In re Solof*, 2 Fed. (2d) 130, 131-132, the Circuit Court of Appeals, Ninth Circuit, said:

> "We will assume, as did the court below, that insolvency was proven, and direct our attention to the remaining question in the case. In this connection, we are admonished that reasonable cause to believe means something more than reasonable cause to suspect.
>
> "'It is not enough that a creditor has some cause to suspect the insolvency of his debtor; but he must have such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency, in order to invalidate a security taken for his debt. To make mere suspicion a ground of nullity in such a case would render the business transactions of the community altogether too insecure. It was never the intention of the framers of the act to establish any such rule. A man may have many grounds of suspicion that his debtor is in failing circumstances, and yet have no cause for a well-grounded belief of the fact. He may be unwilling to trust him further; he may feel anxious about his claim, and have a strong desire to secure it—and yet such belief as the act requires may be wanting. Obtaining additional security, or receiving payment of a debt, under such circumstances is not prohibited by the law. Receiving payment is put in the same category, in the section referred to, as receiving security. Hundreds of men constantly continue to make payments up to the very eve of their failure, which it would be very unjust and disastrous to set aside. And yet

this could be done in a large proportion of cases if mere grounds of suspicion of their insolvency were sufficient for the purpose.' Grant v. First National Bank, 97 U. S. 80, 24 L. Ed. 971. See, also, Stucky v. Masonic Savings Bank, 108 U. S. 74, 2 S. Ct. 219, 27 L. Ed. 640.

"True, the court was there discussing the question of reasonable cause to believe a person insolvent, but the same considerations apply to the question of reasonable cause to believe that a preference was intended. Tumlin v. Bryan, 165 F. 166, 91 C. C. A. 200, 21 L. R. A. (N. S.) 960. The court there said:

" 'But a belief that a debtor is insolvent is a very different thing from the belief referred to by the statute, "reasonable cause to believe that it was intended" by the payments to give a preference. It may often happen that one, though in fact insolvent, will continue his business and make payments in the usual way, without a thought of preferring one creditor to another, and with the hope and belief that he would finally be able to pay all. If these payments were made by the firm, without the thought of injuring other creditors, and in the belief that it would be able to pay them all, the defendant cannot be charged with reasonable cause to believe that a preference was intended. When a debtor pays, and a creditor receives, the amount of a just debt, the natural presumptions are in favor of the good faith of the transaction. To let the mere fact of the bankruptcy of the debtor within four months make the transaction involved voidable would be to create uncertainty and uneasiness as to the probable result of every settlement between debtor and creditor. Reasonable cause to believe that a preference was intended cannot be held to be proved by circumstances that would merely excite suspicion. And circum-

stances may seem suspicious after the bankruptcy occurs that would not appear unusual at the time of their occurrence, and would then have presented no "reasonable cause" on which to found a belief of intended preference. Merchants and other business men constantly continue to make payments up to the very eve of failure, and it would be disastrous to have them set aside on slight proof or mere suspicion.' "

The leading case upon this subject is *Grant v. First National Bank*, 97 U. S. 80, 24 L. Ed. 971. The opinion in this case is quoted more often than that in perhaps any other case. The opinion in part is as follows:

"Some confusion exists in the cases as to the meaning of the phrase, 'having reasonable cause to *believe* such a person is insolvent.' *Dicta* are not wanting which assume that it has the same meaning as if it had read 'having reasonable cause to *suspect* such a person is insolvent.' But the two phrases are distinct in meaning and effect. It is not enough that a creditor has some cause to suspect the insolvency of his debtor; but he must have such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency, in order to invalidate a security taken for his debt. To make mere suspicion a ground of nullity in such a case would render the business transactions of the community altogether too insecure. It was never the intention of the framers of the Act to establish any such rule. A man may have many grounds of suspicion that his debtor is in failing circumstances, and yet have no cause for a well-grounded belief of the fact. He may be unwilling to trust him further; he may feel anxious about his claim and have a strong desire to secure it, and yet such belief as the Act requires may be wanting.

Obtaining additional security, or receiving payment of a debt, under such circumstances is not prohibited by the law. Receiving payment is put in the same category in the section referred to, as receiving security. Hundreds of men constantly continue to make payments up to the very eve of their failure, which it would be very unjust and disastrous to set aside. And yet this could be done in a large proportion of cases if mere grounds of suspicion of their solvency were sufficient for the purpose.

"The debtor is often buoyed up by the hope of being able to get through with his difficulties long after his case is in fact desperate; and his creditors, if they know anything of his embarrassments, either participate in the same feeling, or at least are willing to think that there is a possibility of his succeeding. To overhaul and set aside all his transactions with his creditors, made under such circumstances, because there may exist some grounds of suspicion of his inability to carry himself through, would make the Bankrupt Law an engine of oppression and injustice. It would, in fact, have the effect of producing bankruptcy in many cases where it might otherwise be avoided.

"Hence the Act, very wisely, as we think, instead of making a payment or a security void for a mere suspicion of the debtor's insolvency, requires, for that purpose, that his creditor should have some reasonable cause to believe him insolvent. He must have a knowledge of some fact or facts calculated to produce such a belief in the mind of an ordinarily intelligent man.

"It is on this distinction that the present case turns. It cannot be denied that the officers of the bank had become distrustful of Miller's ability to bring his affairs to a successful termination; and yet it is

equally apparent, independent of their sworn statements on the subject, that they supposed there was a possibility of his doing so. After obtaining the security in question, they still allowed him to check upon them for considerable amounts in advance of his deposits. They were alarmed; but they were not without hope. They felt it necessary to exact security for what he owed them; but they still granted him temporary accommodations. Had they actually supposed him to be insolvent, would they have done this?

"The circumstances calculated to excite their suspicions are very ably and ingeniously summed up in the brief of the appellant's counsel; but we see nothing adduced therein which is sufficient to establish anything more than cause for suspicion. That Miller borrowed money; that he had to renew his note; that he overdrew his account; that he was addicted to some incorrect habits; that he was somewhat reckless in his manner of doing business; that he seemed to be pressed for money, were all facts well enough calculated to make the officers of the bank cautious and distrustful; but it is not shown that any facts had come to their knowledge which were sufficient to lay any other ground than that of mere suspicion. Miller had for years been largely engaged in purchasing, fattening and selling cattle. He had always borrowed money largely to enable him to make his purchases; for this purpose he had long been in the habit of temporarily overdrawing his account; the note which he renewed was not a regular business note, given in ordinary course, but was made to effect a loan from the bank apparently of a more permanent character than an ordinary discount; and his manner of doing business was the same as it had always been. That he was actually insolvent when

the trust deed was executed, there is little doubt; but he was largely indebted in Galesburg, in a different county from that in which Monmouth is situated; and there is no evidence that the officers of the bank had any knowledge of this indebtedness.

"Without going into the evidence in detail, it seems to us that it only establishes the fact that the officers of the bank had reason to be suspicious of the bankrupt's insolvency, when their security was obtained; but that it falls short of establishing that they had reasonable cause to believe that he was insolvent."

Upon this subject the court in *Miller v. Martin*, 17 Fed. (2d) 291, 292-293, said:

"The law is properly laid down in Collier on Bankruptcy (13th Ed.), p. 1328, as follows:

" 'The law presumes that such payments are legal, and the burden of proof is on the trustee, seeking to recover them, to overcome this presumption, and establish the essential elements of a voidable preference. He must prove the insolvency of the debtor at the time the security was given, or the transfer made or recorded, and establish the existence of other creditors of the same class at that time, and that the enforcement of the security or transfer will operate to give them a lesser percentage of their debts than the creditor who receives the transfer or security; and he must also prove the existence of the "reasonable cause to believe," and that the payment dimished the estate of the bankrupt. All this must be done by a fair preponderance of all the evidence in the case, and, where inferences from proved facts are to be drawn, the rule obtains that, if two inferences of substantially equal weight may reasonably be drawn from the proved facts, then that inference shall prevail which sustains the transfer or security.'

"'When the bankruptcy law * * * was enacted, the phrase "reasonable cause to believe," as applied to a preference, had been judicially defined to mean, not mere suspicion, but such knowledge of the facts as to induce a reasonable belief, or cause for well-grounded belief, and such definition followed the phrase into the statute.' City National Bank v. Slocum (C. C. A.) 272 F. 11; citing Grant v. National Bank, 97 U. S. 80, 24 L. Ed. 971; Stucky v. Masonic Bank, 108 U. S. 74, 2 S. Ct. 219, 27 L. Ed. 640; *In re* Eggert (C. C. A.), 102 F. 735; Carey v. Donohue (C. C. A.), 209 F. 328; Baxter v. Ord (C. C. A.), 239 F. 503.

"'In order to invalidate, as a fraudulent preference, within the meaning of the Bankruptcy Act (Comp. St. §§9585-9586), a security taken for a debt, the creditor must have had such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency. It is not sufficient that he had some cause to suspect such insolvency.' Grant v. National Bank, 97 U. S. 80, 24 L. Ed. 971."

In *Hurley v. N. J. Reilly Co.,* 13 Fed. (2d) 466, the opinion is in full as follows:

"This is a proceeding in equity, brought by a trustee in bankruptcy of the Northeastern Shoe Company to recover a preference voidable under section 60b of the Bankruptcy Act (Comp. St. §9644). The material facts as established by the evidence are as follows:

"The bankrupt was engaged in the business of manufacturing shoes. The defendant was a merchant selling leather which entered into the manufacture of shoes. The defendant began doing business with the bankrupt in June, 1924. For the leather first purchased the bankrupt made a partial

payment by check in July, 1924. Other sales were made during July and August, the last sale being made on September 19, 1924. The terms of the sale were 5 per cent 14 days, 4 per cent 30 days, but the defendant did not regard the account as overdue until after the expiration of 60 days from date of invoice. On September 3, 1924, the bankrupt gave a trade acceptance for the amount then due, amounting to $947.99. This trade acceptance became due September 27, 1924, and was not paid. Later certain accounts receivable were assigned by the bankrupt to the defendant, either as payment or security for the indebtedness owed the defendant, which then amounted to $2,085.00. The first assignment was made on or about October 1, 1924. Between that date and October 24, 1924, the bankrupt assigned accounts receivable aggregating in amount $1,889.06. An involuntary petition in bankruptcy was filed November 10, 1924, upon which the Northeastern Shoe Company was adjudicated bankrupt November 24, 1924. I find that at all times between October 1, and October 24, 1924, the period covered by the assignments, the bankrupt was insolvent, and the officers of the company knew, or ought to have known, of such insolvency and that the assignments operated as a preference under section 60a of the Bankruptcy Act. Whether the preference is voidable under section 60b of the Bankruptcy Act is the question presented for consideration.

"As bearing upon this question, the evidence shows that before any sales were made the defendant looked up the credit worth of the bankrupt in a reputable trade journal and found that the bankrupt was entitled to a reasonable amount of credit; when the trade acceptance was not met, the bookkeeper for the defendant called that fact to the attention of Mr. Reilly,

the president and treasurer of the defendant, and, as a result of a telephone conversation with him, the treasurer of the bankrupt agreed to assign the accounts. On September 29, the defendant wrote the plaintiff regarding the unpaid trade acceptance, and on October 1, 1924, received a reply in which the bankrupt stated that they were sorry the trade acceptance had not been met at the bank, but they did not wish to have the defendant become alarmed, as they fully intended to keep their agreement, and in the letter it was suggested that Mr. Reilly come over to the factory on October 6, when they would go over the matter and arrange to settle the account, and also discuss additional orders. On October 2 the defendant wrote the bankrupt that Mr. Reilly would be at their factory Monday morning, as requested, and concludes the letter with this significant paragraph:

"'We are offering some big values in black kid, and we trust you will be in a position to avail yourself of some of our values.'

"Mr. Reilly went to the bankrupt's place of business on October 6, 1924, and looked the plant over: was told by the treasurer of the company that they had a lot of unfilled orders on the books from reputable concerns, and that the outlook for the future was good, if additional working capital could be obtained. Mr. Reilly intimated that he might put some money into the corporation, or at least assist it in obtaining additional capital. No statement as to the financial condition of the company was then forthcoming, but about the 16th day of October the bankrupt's treasurer went to the office of the defendant and presented an approximate statement of the assets and liabilities, which showed a margin of assets over liabilities. Mr. Reilly, with the approval of the bankrupt, arranged with an auditor to investigate the affairs of the bank-

rupt. The auditor took an inventory, examined the books, and found a condition of insolvency, which he reported to Mr. Reilly, who first saw the report some time subsequent to October 24, 1924.

"The real question involved in this case is whether on the facts the defendant had reasonable cause to believe that the assignments would amount to a preference. The fact that the accounts were overdue, and that the trade acceptance had not been paid, would not, standing alone, be sufficient to warrant the court in holding that the defendant had reasonable cause to believe that it was receiving a preference. Voorheis v. National Shawmut Bank, 218 Mass. 69, 105 N. E. 382; McLaughlin v. Fisk Rubber Co. (D. C.), 288 F. 72. But the real question here is whether that fact, coupled with the fact that assignments of accounts were offered and accepted as the only available means of payment, would be sufficient to put a reasonably prudent man upon inquiry.

"It is clear, from representations made by the bankrupt and the conduct of the officers of the defendant, that these officers did actually believe that the bankrupt had a good prospect for the future. They had no reason to suspect that the bankrupt's inability to pay was due to any other cause than its failure to collect outstanding accounts receivable, which, so far as defendant knew, were against customers of good financial standing. There is nothing in the conduct of the defendant to indicate that any distrust respecting the solvency of the bankrupt was entertained. It does not even appear that it entertained a suspicion, but, if the facts excited suspicion, that would not have been sufficient. Collier on Bankruptcy (13th Ed.), p. 1304, and cases cited. It cannot be said as a matter of law that a creditor, who receives in payment or as security assignments of

account, must, as a reasonably prudent business man, be led to the conclusion that the debtor making the assignments is insolvent, especially if other facts and information known to the creditor justify an honest belief in the solvency of the debtor. Assignments of account are becoming more and more common in the commercial world as a means of obtaining working capital, and the modern conception of the practice does not necessarily imply an insolvent condition, or that the other creditors of the debtor of the same class will receive a smaller percentage of their debts. See Matter of Robert Jenkins Corporation (D. C.), 7 Am. Bankr. Rep. (N. S.) 504, 11 F. (2nd) 979.

"I have reached the conclusion, therefore, that when the assignments were made the defendant did not know, and had no reasonable cause to believe, that they would operate as a preference. The plaintiff, therefore, is not entitled to avoid the preference, and cannot prevail in this suit."

In *Closson v. Newberry's Hardware Co.,* 283 Fed. 33, the Circuit Court of Appeals, 8th Circuit, held that knowledge by a creditor that a business in which the bankrupt corporation was engaged had been seriously crippled by the ending of the war, that the bankrupt was experiencing difficulty in continuing its business because of lack of a market for its product and that it was having difficulty also in securing ready money is insufficient to show that the creditor had reasonable cause to believe a payment to him by the bankrupt would effect a preference.

The opinion in *Sumner v. Parr,* 270 Fed. 675, reads as follows:

"Although the evidence of the bankrupt's insolvency of May 29th is absent, strictly speaking, I shall disregard that feature of the case, and assume

that the only issue left open is of the defendant's knowledge that the transfer would result in giving him a preference. He knew that the bankrupt had been doing a prosperous business, and had had very substantial, if not large, interests in real property. He knew that she had been slow in her payments for some time, and that he had been obliged to take notes from her, first for $500, and finally, in the autumn of 1917, for $1,000. He necessarily knew, as he had repeatedly asked her to pay up, that she did not have enough ready money to do so. In other words, he knew that she was getting into an embarrassed financial condition. In taking the notes, he says his chief purpose was not to have so much money outstanding without interest, and this was undoubtedly so; but in taking security he was certainly actuated by suspicion of the continued sufficiency of his debtor's circumstances. He knew also that her total indebtedness amounted to some $6,000 or $7,000; in fact, it probably was $2,000 or $3,000 greater than this; but there is no evidence that he knew of any more, and, as she had told him what the facts were, I think he might reasonably have rested without further inquiry.

"He also knew of the extent of her assets. These assets consisted of equities in various pieces of real property; but there is throughout the case not a scintilla of evidence to show what was the real value of those equities, except the fact that when sold under the hammer they produced little or nothing. I cannot accept this proof as equivalent to a showing of what their value was. Even if it may be some evidence of value, the values of real property, as they are estimated by experts and are relied upon in general, are in no sense determined by what the property will bring at auction. Therefore, while the defendant

knew the assets, there is no evidence of their value, nor can I tell what he would have found it to be if, using the information she gave him, he had made inquiry of qualified experts. The Twenty-third street property alone had had an equity of some $33,000 over a mortgage of $17,000 seven years before. It may have dwindled to nothing, but I have no means of telling what it was, except the fact that it brought deficiency upon foreclosure. The same thing in general is true of the other pieces of property, all of which had substantial values some time before. If I am to take notice that real estate values in New York had gone off enormously, I should also observe that the shrinkage was perhaps at its lowest in the spring of 1918. The difficulty with the case in this aspect is that the plaintiff, on whom the burden rests, has not given any proof from which those values could be ascertained.

"Therefore the defendant's knowledge may be put in this form: There were no immediate suspicious circumstances. Nothing had just happened which should have caused him to suppose that the bankrupt was any nearer to insolvency than she had been for some time past. Finding his debtor unable to make ready payments, and knowing that she had substantial property, he became suspicious, and dissatisfied with the delays, and took security. If this charges him with knowledge that the security will create a preference, then so is every creditor who takes security because he has become doubtful and suspicious of the eventful insolvency of his debtor. When the statute requires belief that a preference will result, it means more than this; for the taking of security only shows that the creditor has cause to believe that a preference might result. The two are very different. It may be the difference is only one of degree,

but the statute establishes it none the less. In this case the proof goes no further than to show that it might.

"The defendant may take a decree, but, under the circumstances, without costs."

In *In re Union Hill Preserving Co.*, 1 Fed. (2d) 415, it appears that an officer of the debtor's bank had advised claimant that the debtor was in financial straits and that the bank would make no further advances to the debtor. The court said:

". . . this meager information did not import knowledge of insolvency, nor afford reasonable ground for believing that a preference was intended by the sale of the apples and cherries, when the bankrupt already had the money therefor."

VI. Conclusion.

Many more decisions could be cited, but we believe that those already cited and quoted from fairly state the law applicable to this case. From them certain conclusions may be drawn, viz.:

1. It is the policy of the law to protect honest business transactions;

2. The law presumes that the payments in question are legal and do not constitute a preference, and the burden of proof to establish the contrary is on appellee.

3. If two inferences may reasonably be drawn from proved facts, then that inference shall prevail which sustains the payments. (*Miller v. Martin, supra.*)

4. "Reasonable cause to believe" means something just short of actual knowledge; it means more than reasonable cause to suspect.

5. Facts sufficient to cause a creditor to be cautious as to future transactions or to require security for a past indebtedness are insufficient in themselves to establish reasonable cause to believe that the debtor is insolvent.

6. Failure to pay a debt or obligation when due is not sufficient in itself to establish such reasonable cause to believe. (*Hurley v. N. J. Reilly Co., supra.*)

7. That the creditor knew that his debtor was having difficulty in securing ready money is insufficient to show that the creditor had such reasonable cause to believe. (*Closson v. Newberry's Hardware Co., supra.*)

8. That the Farmers and Merchants National Bank would not lend more money to the bankrupts is insufficient to establish such probable cause. (*In re Union Hill Preserving Co., supra.*)

We conclude our argument with a further quotation from the decision in *In re Solof,* 2 Fed. (2d) 130, 132:

> ". . . Counsel for appellant directs our attention to a large number of, what he terms, 'badges of reasonable cause to believe,' such as information contained in a financial statement; advice to the debtor to make no large payments to creditors; to make payments on a *pro rata* basis only; refusal to ship further goods; accepting return of merchandise; information that creditors were pressing; protested checks and trade acceptances; requirement that payments be made in cash or by cashier's check; extensions requested; failure to inspect books when the opportunity presented itself; and an intimate knowledge of the business affairs of the debtors. All these circumstances may, and doubtless do, indicate that the creditor was apprehensive as to its claim; but they do not necessarily prove that it had reasonable cause

to believe that a preference was intended. Other testimony in the case throws some light on the general situation. The bankrupts had conducted a large and extensive business for some years prior to bankruptcy. So far as the record discloses, no question as to their financial standing arose until late in the year 1922 or early in 1923. They continued to conduct their business in the usual and ordinary course up to the filing of the involuntary petition against them. During the four months' period, or between February 1 and June 6, 1923, they paid to creditors on open account, notes payable, and trade acceptances, the sum of approximately $168,000, and purchased merchandise, on credit, to the amount or value of approximately $111,000. Were creditors to whom these vast sums were paid all preferred, and were wholesalers selling merchandise on credit to a concern of known insolvency or even of questionable solvency? These questions suggest their own answer. It may be urged that the appellee had knowledge of facts not possessed by other creditors, but we are not convinced that such was the case. In any event, it cannot be said that a creditor receiving approximately 50 per cent of its claim, in 26 different payments running over a period of four months, had reasonable cause to believe that a preference would result or was intended."

It is respectfully submitted that the findings of the referee are not supported by the evidence, that his order is erroneous and that the Honorable Wm. P. James, District Judge, erred in approving and confirming the referee's order.

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